PROTECTING OLDER AMERICANS AGAINST OVERPAYMENT OF INCOME TAXES

(Deductions and credits you are entitled to use for 2004)

UNITED STATES SENATE SPECIAL COMMITTEE ON AGING REPORT

The Senate Special Committee on Aging is issuing this tax information paper for tax year 2004 with older Americans in mind. The Committee has included a checklist for itemized deductions such as medical and dental expenses; a standard deduction table; and information about how to ask the IRS for help when filing your tax returns.

Gordon H. Smith,

Chairman

WHO MUST FILE--BY FILING STATUS AND GROSS INCOME

Generally, even though you owe no tax you must file a tax return if your gross income for the year is at least as much as the amount shown for your filing status and age on the table below:

Filing Status and Age	2004 Gross Income
Single	
Under 65	$7,950.
65 or older	9,150.
Married Filing Joint Return	
Both spouses under 65	15,900.
One spouse 65 or older	16,850.
Both spouses 65 or older	17,800.
Married Filing Separate Return	
(or living apart from spouse at end of year or on date spouse died) All regardless of age	3,100.
Head of Household	
Under 65	10,250.
65 or older	11,450.
Qualifying Widow(er) with Dependent Child	
Under 65	12,800.
65 or older	13,750.

Even if your income is less than the amount as indicated earlier you must file a return if in 2004:

- you received any advance earned income credit (EIC) payments from your employer(s);
- you were self-employed and had net earnings of at least $400;
- you had wages of $108.28 or more from a church or qualified church-controlled organization that is exempt from employer Social Security and Medicare taxes;
- you owe any tax on a qualified retirement plan, an individual retirement account (IRA), or on an Archer medical savings account (MSA);
- you owe alternative minimum tax;
- you owe tax on a Coverdell ESA or on qualified tuition program earnings;
- you owe uncollected Social Security, Medicare or railroad retirement tax on group-term life insurance, or Social Security, Medicare or railroad retirement tax on tips you did not report to your employer; or
- you owe any tax from recapture of investment credit or a low-income housing credit you claimed in previous years, recapture tax on the disposition of a home purchased with a federally-subsidized mortgage, a qualified electric vehicle credit, an education credit, Indian employment credit or new market credit.

Note: You must file a tax return to obtain a refund of any taxes you overpaid for 2004 or if you qualify for the earned income credit or the additional child tax credit. If you turned age 65 on January 1, 2005, you are considered to be age 65 for tax year 2004.

FILING DEADLINE

The filing deadline for 2004 income tax returns is midnight, Friday, April 15, 2005. Any return postmarked after April 15 may be subject to tax penalties unless you file for extension by the filing date. You can get an automatic 4-month extension if, by April 15, 2005, you either file Form 4868, or use one of the three E-file options. If you expect to owe tax with your 2004 return, you may pay all or part of it by phone using your American Express, Discover, MasterCard, or VISA credit card. If you pay by credit card the service provider will charge a convenience fee based on the amount of your payment. These fees may vary by provider. In some instances an additional 2-month extension of time may be granted. An extension of more than 6 months is generally not approved if you are living in the United States.

WHICH FORM TO FILE

FORM 1040EZ

Form 1040EZ is used only by those who can file as single or married filing jointly and who are under age 65 and not blind. You cannot claim any dependents, any adjustments to income (such as an IRA contribution or student loan interest deduction), any itemized deductions, or any tax credits (other than the earned income credit). All your income must come from wages, salaries, tips, unemployment compensation, Alaska Permanent Fund dividends, taxable scholarship and fellowship grants, qualified state tuition program earnings, and taxable interest of $1,500 or less. Your taxable income must be less than $100,000. You cannot have received any advance earned income credit or owe employment taxes for wages paid to a household emploee..

FORM 1040A

Form 1040A can be used by any filing status. Your taxable income must be less than $100,000. You can use the form to report distributions received from individual retirement accounts (IRAs), pension and annuity payments, taxable Social Security or equivalent Railroad Retirement benefits, wages, salaries, tips, taxable scholarship and fellowship grants, interest, ordinary dividends (including Alaska Permanent Fund dividends), capital gains distributions, qualified state tuition program earnings, and unemployment compensation. The only adjustments to income on Form 1040A are the deductions for educator expenses, contributions to an IRA, tuition and fees deduction, or the student loan interest deduction. Your taxes may only be from the tax table, the alternative minimum tax, an advance earned income credit payment, recapture of an education credit, form 8615 (Tax for Children Under Age 14 Who have Investment Income of More Than $1,600), or the capital gain tax worksheet. You can take certain credits when using this form, such as the earned income credit, the credit for child and dependent care expenses, the credit for the elderly or the disabled, the child tax credit, the additional child tax credit, the education credits, the retirement savings contributions credit, and the adoption tax credit.

FORM 1040

Form 1040 is used by all other individuals (except nonresident aliens). It must be used if your taxable income is $100,000 or more, or you itemize your deductions such as home mortgage interest, charitable contributions, taxes, medical and dental expenses, etc. Capital gains or losses from the sale or exchange of capital assets or business property can be reported only on Form 1040. If you owe self-employment tax (see Schedule SE), you must use Form 1040. Form 1040 is also used if you have to recapture an investment credit, a low-income housing credit, a qualified electric vehicle credit, or an Indian employment credit. This form is also used if you must pay household employment taxes. Frequently this form is used when you have to file other forms with your return to report certain exclusions, taxes, or transactions.

SOCIAL SECURITY BENEFITS

Some individuals will not be taxed on any of their social security benefits. Others may have to include a portion of their Social Security benefits (up to 85% in some cases) in taxable income. Generally, the greater a taxpayer's income, the greater the portion of their benefits that are includible in taxable income.

You should receive Form SSA-l099,Social Security Benefit Statement, if you received benefits in 2004. To estimate quickly whether you must include any of your benefits in taxable income, add up your income from all sources, including any tax-exempt interest you may have received, plus one-half of your net benefits. If your total income from all sources is **not** more than the following base amounts, your benefits generally are not taxable:

- $25,000 if you are single, head of household, or qualifying widow(er),
- $32,000 if you are filing a joint return, or
- $-0- if you are married filing a separate return and lived with your spouse at any time during 2004 ($25,000 if you lived apart from your spouse for all of 2004).

For more information, get IRS Publication 915, "Social Security and Equivalent Railroad Retirement Benefits."

TAX WITHHOLDING AND ESTIMATED TAX PAYMENTS FOR 2004

Unless you choose not to have any tax withheld, federal income tax will generally be taken from the taxable part of your pension and annuity payments. This includes distributions from an IRA, from a life insurance company under an endowment, annuity, or life insurance contract, or from a pension, annuity, profit-sharing or stock bonus plan, or any similar plan that defers the time you receive compensation. However, your right to choose not to have tax withheld applies only to a distribution other than an "eligible rollover distribution" from an employer retirement plan. Employers must withhold tax at a rate of 20% on distributions not directly transferred to another eligible plan trustee.

To tell the company that pays your pension or annuity (that is not an "eligible rollover distribution") how much you want withheld, fill out Form W-4P, or a similar form provided by the payer, showing your marital status and the number of withholding allowances to which you are entitled. If you do not give the payer a Form W-4P, tax will be withheld as if you are married and are claiming three withholding allowances. You may also use this form to tell the payer you do not want any tax withheld. However, if you are a U.S. citizen or resident alien whose address is outside the U.S. or its possessions, the payer must withhold tax.

Tax is withheld at the rate of 10% on nonperiodic payments and at the rate of 20% on any part of an "eligible rollover distributions" that is not rolled over directly to another qualified plan. See Chapter 1 of IRS Publication 505, "Tax Withholding and Estimated Tax," for the withholding rules on periodic and nonperiodic payments and on eligible rollover distributions.

Remember, if no tax or not enough tax is withheld from your income, you may need to make quarterly payments of estimated tax. Your estimated tax generally is the total of your expected income tax, self-employment tax, and other taxes (such as employment taxes for household workers) that you will owe, less your withholding and tax credits.

If your withholding and/or estimated tax deposits are significantly less than your tax liability, you may be subject to estimated tax penalties. In general, no penalty will apply if your tax year 2004 return shows a balance due of less than $1,000. Also, no penalty will apply if your deposits for 2004 exceed (1) 90% of your 2004 tax (i.e., total tax less credits) or (2) 100% of the tax shown on your prior year's return (110% of your 2004 tax if your adjusted gross income for 2004 exceeds $150,000 or $75,000 if married filing separately). Get Form 1040-ES, "Estimated Tax for Individuals" (it has a worksheet) to see if you have to make estimated tax payments for tax year 2005.

EXEMPTIONS

You are allowed a $3,100 deduction for each exemption shown on your tax return. If your adjusted gross income exceeds $214,050 for joint returns, $142,700 for single returns, $178,350 for head-of-household returns, or $107,025 for married persons filing separately, you may lose the benefit of part or all of your exemptions. In general, a person may be claimed as a dependent of another taxpayer, provided five tests are met: (1) support, (2) gross income, (3) member of household or relationship, (4) citizen or resident, and (5) joint return. For more information, get Publication 501, "Exemptions, Standard Deduction, and Filing Information." If you can be claimed as a dependent on the tax return of another taxpayer, you cannot claim your exemption on your own tax return.

STANDARD DEDUCTION

The standard deduction reduces the need for many taxpayers to itemize their deductions. The standard deduction, which depends on your filing status and whether you are age 65 or older or blind, is figured separately. Once you have figured your standard deduction amount, you should then decide which gives you a higher tax benefit---taking the standard deduction or itemizing your deductions on Schedule A of Form 1040.

If you are age 65 or older or blind in 2004, your standard deduction is higher. You are considered 65 for the 2004 tax year if your 65th birthday was on or before January 1, 2005. You are considered blind for 2004 if you are blind on the last day of 2004. Your tax instruction booklet has more information.

Special rules. Your standard deduction is zero if your spouse itemizes deductions on a separate return, you are a dual-status or nonresident alien, or you have a short tax year. If you can be claimed as a dependent on another person's tax return, your standard deduction may be limited. If you meet one of these special rules, you may not use the following standard deduction table. See your tax instruction booklet for more details.

2004 Standard Deduction Table

Check the number of boxes that apply to you.

You	❏	65 or older	❏	Blind	❏
Your spouse	❏	65 or older	❏	Blind	❏

Total number of boxes you checked. . . . . ❏

If your filing status is:	Number of boxes checked	Your standard deduction is:
Single	1	$6,050
	2	$7,250
Married filing jointly or Qualifying Widow(er) with dependent child	1	$10,650
	2	$11,600
	3	$12,550
	4	$13,500
Married filing separately	1	$5,800
	2	$6,750
	3	$7,700
	4	$8,650
Head of Household	1	$8,350
	2	$9,550

CHECKLIST OF ITEMIZED DEDUCTIONS FOR SCHEDULE A (FORM 1040)

If your adjusted gross income (AGI) is more than $142,700 ($71,350 if you are married filing separately), the amount of certain itemized deductions may be limited.

MEDICAL AND DENTAL EXPENSES

Medical and dental expenses include payments you make for the diagnosis, cure, relief, treatment, or prevention of disease or for treatment affecting any part or function of the body. You may include transportation expenses incurred for, and essential to, needed medical care. If you do not want to use your actual expenses, you can use a standard rate of 14 cents a mile for use of your car. Unreimbursed medical expenses are deductible to the extent they are more than 7.5% of your AGI (line 35, Form 1040). Expenses may be deducted only in the year you paid them. If you charge medical expenses on your credit card, include the expenses in the year the charge is made.

You may generally include payments for qualified long-term care contracts and expenses for unreimbursed costs for qualified long-term care of chronically ill individuals. Benefits from long-term care insurance are generally excluded from your income. For more information, get IRS Publication 502, "Medical and Dental Expenses."

TAXES

In the case of a cash-basis taxpayer, taxes are deductible in the year when paid. Business taxpayers can deduct state, local, and foreign taxes to the extent they are attributable to a trade, or business, or when they are incurred for property held for the production of rents or royalties. Some examples of deductible taxes are:

- personal property taxes based on value,
- state, local, or foreign income tax,
- state, local, or foreign real estate taxes when based on the assessed value of the property, and
- state and local general sales taxes*

*Beginning in 2004, taxpayers will have the option of electing to deduct state and local general sales taxes, <u>instead of</u> state and local income taxes. Taxpayers can deduct either their actual sales tax expenses or the applicable amount from the Optional State Sales Tax Tables provided in IRS Publication 600. In addition to the tax table amount, taxpayers may be able to also deduct state and local sales tax paid on motor vehicles, boats and other items specified in IRS Publication 600. The additional deductible amount may not exceed the amount that would be imposed at the general sales tax rate.

INTEREST

You cannot deduct the interest you paid on loans used for personal purposes, other than qualified home mortgage interest. In most cases, you will be able to deduct all of your home mortgage interest. However, there are limits on home mortgages and home equity line-of-credit mortgages. Additional information can be found in IRS Publication 936, "Home Mortgage Interest Deduction." Beginning in 2003, the deduction for student loan interest is no longer subject to the 5-year repayment period. In addition, the modified adjusted gross income level at which your deduction is reduced or eliminated has been increased. This deduction is explained in IRS Publication 970, "Tax Benefits for Higher Education."

CHARITABLE CONTRIBUTIONS

A charitable contribution is a contribution or gift to, or for the use of, a qualified organization. Qualified organizations include non-profit groups that use their funds for religious, charitable, educational, scientific, or literary purposes, or organizations that work to prevent cruelty to children or animals. An organization can tell you if it is a qualified organization. In the case of cash contributions of $250 or more, the donation must be substantiated by a contemporaneous written acknowledgment from the non-profit organization. To deduct your contributions, you must file Form 1040 and itemize deductions on Schedule A.

You generally can deduct your contributions only in the year that you actually make them in cash or other property. Contributions of property (clothing, books, furniture, etc.) generally are deducted at their fair market value, but in certain cases, your deduction is limited to less than fair market value. If you claim a deduction for over $500 in noncash contributions, you must file Form 8283, "Noncash Charitable Contributions." You may want to get IRS Publication 526, "Charitable Contributions" (for individuals), and IRS Publication 561, "Determining the Value of Donated Property."

Note: Beginning in 2005, the deduction for donations of motor vehicles that are sold by charitable recipient generally will be limited to the greater of $500 or the amount received by the charity from the sale of the motor vehicle. See IRS Publication 561 for more information.

CASUALTY OR THEFT LOSSES

You may deduct casualty losses, such as those that result from a tornado, flood, storm, fire, or auto accident (provided it was not caused by a willful act or willful negligence), or theft losses. Your casualty loss is generally the lesser of (1) the decrease in fair market value of the property as a result of the casualty or theft, or (2) your adjusted basis in the property before the casualty

Earned Income Credit in a Nutshell

First, you must meet all the rules in this column.	Second, you must meet all the rules in one of these columns, whichever applies.			Third, you must meet the rules in this column.
Rules for Everyone	Rules If You Have a Qualifying Child		Rules If You Do Not Have a Qualifying Child	Figuring and Claiming the EIC
1. Your adjusted gross income (AGI) must be less than: • $34,458 ($35,458 for married filing jointly) if you have more than one qualifying child, • $30,338 ($31,338 for married filing jointly) if you have one qualifying child, or • $11,490 ($12,490 for married filing jointly) if you do not have a qualifying child.	2. You must have a valid social security number. 3. Your filing status cannot be "Married filing separately." 4. You must be a U.S. citizen or resident alien all year. 5. You cannot file Form 2555 or Form 2555-EZ (relating to foreign earned income). 6 Your investment income must be $2,650 or less. 7. You must have earned income.	8. Your child must meet the relationship, age, and residency tests. 9. Your qualifying child cannot be used by more than one person to claim the EIC. 10. You cannot be a qualifying child of another person.	11. You must be at least age 25 but under age 65. 12. You cannot be the dependent of another person. 13. You cannot be a qualifying child of another person. 14. You must have lived in the United States more than half of the year.	15. Your earned income must be less than: • $34,458 ($35,458 for married filing jointly) if you have more than one qualifying child • $30,338 ($31,338 for married filing jointly) if you have one qualifying child, or • $11,490 ($12,490 for married filing jointly) if you do not have a qualifying child.

or theft. This amount must be reduced by any insurance or other reimbursement you receive. Special provisions are available for losses from a disaster occurring in a presidentially declared disaster zone (such as the World Trade Center).

Casualty and theft losses to income-producing property are figured in Section B of Form 4684. Your non-business casualty or theft losses are deductible only to the extent that your total losses during the year exceed 10% of your adjusted gross income after reducing each separate casualty or theft by $100. You must use Section A of Form 4684 to figure your personal use property casualty or theft loss. Report your casualty or theft loss on line 19 of Schedule A (Form 1040).

You may not deduct a casualty or theft loss that is covered by insurance unless you filed a timely insurance claim for reimbursement. However, even if you did not file an insurance claim, you may deduct the part of the loss not covered by insurance. For more information, see IRS Publication 547, "Casualties, Disasters, and Thefts (Business and Nonbusiness)."

MISCELLANEOUS DEDUCTIONS

Unreimbursed employee business expenses, expenses of producing income, and other qualifying expenses are deducted as miscellaneous itemized deductions on Schedule A (Form 1040). Some miscellaneous itemized deductions cannot be deducted in full. You can claim the amount of expenses that is more than 2% of your adjusted gross income. In general, you apply the 2% limit after you apply any other deduction limit.

TAX CREDITS

CREDIT FOR DEPENDENT CARE EXPENSES

Part of your payments made for dependent care may be claimed as a credit against tax. In the case of an elderly dependent, if the dependent spends at least eight hours a day in the taxpayer's home, expenditures made for out of home, noninstitutional care are eligible for the credit. Dependent care centers must be in compliance with all state and local regulations for the taxpayer to count such expenditures toward qualified expenses. Married couples must file a joint return to be eligible for the credit. See IRS Publication 503, "Child and Dependent Care Expenses" for more information.

CREDIT FOR THE ELDERLY OR THE DISABLED

You may be able to claim this credit if you are: (1) age 65 at the end of the tax year or older or (2) under age 65 at the end of the tax year and retired on a permanent and total disability for which you received taxable disability benefits in 2004 and you did not reach mandatory retirement age during the year. The credit is based in part on your filing status and adjusted gross income (AGI). Generally, you cannot claim a credit if you are: (1) single, head of household, or qualifying widower if your AGI is $17,500 or more; (2) married filing jointly with only one spouse eligible and your AGI is $20,000 or more; (3) married filing jointly with both spouses eligible and your AGI is $25,000 or more; or (4) married filing separately and your AGI is $12,500 or more.

For more information, see IRS Publication 524, "Credit for the Elderly or the Disabled."

EARNED INCOME CREDIT

The earned income credit (EIC) is a special credit for low and moderate income workers. If you are age 65 or older you are not eligible for this credit. You are not allowed to claim the credit if your investment income for 2004 exceeds $2,650.

You can receive an advance payment of the earned income credit in your paycheck throughout the year. To get the advance payment, fill out Form W-5 and give it to your employer.

Additional information can be obtained from IRS Publication 596, "Earned Income Credit," and the instructions for Form W-5.

SIGNATURE

When you have completed your return, be sure to sign and date it. If it is a joint return, both spouses must sign.

IRS ASSISTANCE IS AVAILABLE TO HELP YOU

Publications to assist you: The IRS prepares many free publications to help answer your tax questions. Besides the general Publication 17, "Your Federal Income Tax," publications are available on specific topics, such as:

PUBLICATION NUMBERS AND TITLES

1 .... Your Rights as a Taxpayer
502.... Medical and Dental Expenses
505.... Tax Withholding and Estimated Tax
523.... Selling Your Home
524.... Credit for the Elderly or the Disabled
530.... Tax Information for First-Time Homeowners
554.... Older Americans' Tax Guide
559.... Survivors, Executors, and Administrators
575.... Pension and Annuity Income
590.... Individual Retirement Arrangements (IRAs) (Including Roth IRAs and Education IRAs)
721.... Tax Guide to U.S. Civil Service Retirement Benefits
907.... Tax Highlights for Persons with Disabilities
910.... Guide to Free Tax Services
915.... Social Security and Equivalent Railroad Retirement Benefits
939.... General Rule for Pensions and Annuities
950.... Introduction to Estate and Gift Taxes
2053.. Quick and Easy Access to IRS Tax Help and Products

IRS publications can be ordered by mail, using the order form in your tax package, or by calling IRS toll-free at 1-800-829-3676. In addition, the Bank, Post Office and Library (BPOL) Tax Form Distribution Program is a voluntary program created to provide taxpayers with access to tax forms and related products in their local communities.

Tele-Tax: The IRS has a telephone service which provides recorded tax information, from tapes on such areas as IRS services-Volunteer tax assistance, and outreach programs, Tax Assistance for Individuals with Disabilities and the Hearing Impaired, Change of Address-How to Notify IRS, Electronic Filing, Highlights of Tax Changes, Power of Attorney Information, Decedents, Pensions-The General Rule and the Simplified Method, and Lump-Sum Distributions. Tele-Tax is available 24 hours a day, 7 days a week, to taxpayers who use touch-tone telephones (1-800-829-4477). Tele-Tax topics are also available using a personal computer and modem (connect to http://www.irs.gov. Through Tele-Tax Refund Information service, you can also check on the status of your refund.

Other special IRS programs offering free assistance: Through the tax counseling for the elderly (TCE) program, IRS-trained volunteers assist individuals age 60 or older with their tax returns at neighborhood locations in many areas. In addition, certain volunteer income tax assistance (VITA) aides have been trained to help older Americans with their tax returns. (VITA assistance is also available to persons who are low income, have disabilities, or are non-English-speaking.) To find the location of the VITA or TCE site nearest to you, call 1-800-829-1040. The locations of an American Association of Retired Persons (AARP) Tax-Aide site can be found by calling 1-888-AARPNOW and entering, when prompted, your 5-digit zip code, or visiting their Internet site at http://www.aarp.org/taxaide/home.html.